

AMENDED IN SENATE MAY 1, 2003  
AMENDED IN SENATE MARCH 17, 2003

**SENATE BILL**

**No. 4**

**Introduced by Senator Hollingsworth**

December 2, 2002

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An act to ~~amend Sections 17041 and 17062 of~~ *add Section 17140.6* to the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

SB 4, as amended, Hollingsworth. ~~Personal income taxes: rates: reduction~~ *Income taxes: exclusion: military: widows and children.*

*The Personal Income Tax Law imposes a tax with respect to gross income, as defined, and provides various exclusions from gross income.*

*This bill would provide an exclusion from gross income for qualified interest, as defined, received by a widow or any child of an individual that was on active duty and died in combat, as specified.*

*This bill would take effect immediately as a tax levy.*

~~The Personal Income Tax Law imposes a tax upon taxable income at various rates depending upon the amount of that income, and also imposes an alternative minimum tax based upon specified tax preference items.~~

~~This bill would, commencing with taxable years beginning on or after January 1, 2003, reduce all marginal tax rates, as provided, and would eliminate the tax on taxable income and the alternative minimum tax for taxable years beginning on or after January 1, 2007.~~

~~This bill would take effect immediately as a tax levy.~~

Vote: majority. Appropriation: no. Fiscal committee: yes.  
State-mandated local program: no.

*The people of the State of California do enact as follows:*

1 ~~SECTION 1. Section 17041 of the Revenue and Taxation~~  
2 ~~Code is amended to read:~~

3 *SECTION 1. Section 17140.6 is added to the Revenue and*  
4 *Taxation Code, to read:*

5 *17140.6. (a) For each taxable year beginning on or after*  
6 *January 1, 2003, gross income does not include an amount equal*  
7 *to the amount of qualified interest received by a widow or any child*  
8 *of an individual that was on active duty with any branch of the*  
9 *Armed Forces of the United States and died in combat.*

10 *(b) For purposes of this section, "qualified interest" means any*  
11 *interest that accrued prior to payment on amounts payable under*  
12 *an insurance policy provided by the Armed Forces of the United*  
13 *States as a result of the death specified in subdivision (a).*

14 *SEC. 2. This act provides for a tax levy within the meaning of*  
15 *Article IV of the Constitution and shall go into immediate effect.*

16 ~~17041. (a) There shall be imposed for each taxable year upon~~  
17 ~~the entire taxable income of every resident of this state who is not~~  
18 ~~a part-year resident, except the head of a household as defined in~~  
19 ~~Section 17042, taxes in the following amounts and at the following~~  
20 ~~rates upon the amount of taxable income computed for the taxable~~  
21 ~~year as if the resident were a resident of this state for the entire~~  
22 ~~taxable year and for all prior taxable years for any carryover items,~~  
23 ~~deferred income, suspended losses, or suspended deductions:~~

24		
25	If the taxable income is:	———— The tax is:
26	Not over \$3,650 .....	1% of the taxable income
27	Over \$3,650 but not	
28	over \$8,650 .....	\$36.50 plus 2% of the excess over
29		\$3,650
30	Over \$8,650 but not	
31	over \$13,650 .....	\$136.50 plus 4% of the excess over
32		\$8,650
33	Over \$13,650 but not	
34	over \$18,950 .....	\$336.50 plus 6% of the excess over
35		\$13,650

Over \$18,950 but not	
—over \$23,950 .....	\$654.50 plus 8% of the excess over
	\$18,950
Over \$23,950 .....	\$1,054.50 plus 9.3% of the excess
	over \$23,950

~~(b) (1) There shall be imposed for each taxable year upon the taxable income of every nonresident or part-year resident, except the head of a household as defined in Section 17042, a tax as calculated in paragraph (2).~~

~~(2) The tax imposed under paragraph (1) shall be calculated by multiplying the “taxable income of a nonresident or part-year resident,” as defined in subdivision (i), by a rate (expressed as a percentage) equal to the tax computed under subdivision (a) on the entire taxable income of the nonresident or part-year resident as if the nonresident or part-year resident were a resident of this state for the taxable year and as if the nonresident or part-year resident were a resident of this state for all prior taxable years for any carryover items, deferred income, suspended losses, or suspended deductions, divided by the amount of that income.~~

~~(c) There shall be imposed for each taxable year upon the entire taxable income of every resident of this state who is not a part-year resident for that taxable year, when the resident is the head of a household, as defined in Section 17042, taxes in the following amounts and at the following rates upon the amount of taxable income computed for the taxable year as if the resident were a resident of the state for the entire taxable year and for all prior taxable years for carryover items, deferred income, suspended losses, or suspended deductions:~~

If the taxable income is:	———— The tax is:
Not over \$7,300 .....	1% of the taxable income
Over \$7,300 but not	
—over \$17,300 .....	\$73 plus 2% of the excess
	over \$7,300
Over \$17,300 but not	
—over \$22,300 .....	\$273 plus 4% of the excess
	over \$17,300

1	Over \$22,300 but not	
2	—over \$27,600 .....	\$473 plus 6% of the excess
3		over \$22,300
4	Over \$27,600 but not	
5	—over \$32,600 .....	\$791 plus 8% of the excess
6		over \$27,600
7	Over \$32,600 .....	\$1,191 plus 9.3% of the excess over
8		\$32,600

(d) (1) There shall be imposed for each taxable year upon the taxable income of every nonresident or part-year resident when the nonresident or part-year resident is the head of a household, as defined in Section 17042, a tax as calculated in paragraph (2).

(2) The tax imposed under paragraph (1) shall be calculated by multiplying the “taxable income of a nonresident or part-year resident,” as defined in subdivision (i), by a rate (expressed as a percentage) equal to the tax computed under subdivision (a) on the entire taxable income of the nonresident or part-year resident as if the nonresident or part-year resident were a resident of this state for the taxable year and as if the nonresident or part-year resident were a resident of this state for all prior taxable years for any carryover items, deferred income, suspended losses, or suspended deductions, divided by the amount of that income.

(e) There shall be imposed for each taxable year upon the taxable income of every estate, trust, or common trust fund taxes equal to the amount computed under subdivision (a) for an individual having the same amount of taxable income.

(f) The tax imposed by this part is not a surtax.

(g) (1) Section 1 (g) of the Internal Revenue Code, relating to certain unearned income of minor children taxed as if the parent’s income, shall apply, except as otherwise provided.

(2) Section 1(g)(7)(B)(ii)(II) of the Internal Revenue Code, relating to income included on parent’s return, is modified, for purposes of this part, by substituting “1 percent” for “15 percent.”

(h) For each taxable year beginning on or after January 1, 1988, the Franchise Tax Board shall recompute the income tax brackets prescribed in subdivisions (a) and (c). That computation shall be made as follows:

1 ~~(1) The California Department of Industrial Relations shall~~  
2 ~~transmit annually to the Franchise Tax Board the percentage~~  
3 ~~change in the California Consumer Price Index for all items from~~  
4 ~~June of the prior calendar year to June of the current calendar year,~~  
5 ~~no later than August 1 of the current calendar year.~~

6 ~~(2) The Franchise Tax Board shall do both of the following:~~

7 ~~(A) Compute an inflation adjustment factor by adding 100~~  
8 ~~percent to the percentage change figure that is furnished pursuant~~  
9 ~~to paragraph (1) and dividing the result by 100.~~

10 ~~(B) Multiply the preceding taxable year income tax brackets by~~  
11 ~~the inflation adjustment factor determined in subparagraph (A)~~  
12 ~~and round off the resulting products to the nearest one dollar (\$1).~~

13 ~~(i) The income tax rates prescribed in subdivisions (a) and (c)~~  
14 ~~shall be modified as follows:~~

15 ~~(1) For any taxable year beginning on or after January 1, 2003,~~  
16 ~~and before January 1, 2004, 1 percent shall be 0.80 percent, 2~~  
17 ~~percent shall be 1.6 percent, 4 percent shall be 3.2 percent, 6~~  
18 ~~percent shall be 4.8 percent, 8 percent shall be 6.4 percent, and 9.3~~  
19 ~~percent shall be 7.44 percent.~~

20 ~~(2) For any taxable year beginning on or after January 1, 2004,~~  
21 ~~and before January 1, 2005, 1 percent shall be 0.60 percent, 2~~  
22 ~~percent shall be 1.2 percent, 4 percent shall be 2.4 percent, 6~~  
23 ~~percent shall be 3.6 percent, 8 percent shall be 4.8 percent, and 9.3~~  
24 ~~percent shall be 5.58 percent.~~

25 ~~(3) For any taxable year beginning on or after January 1, 2005,~~  
26 ~~and before January 1, 2006, 1 percent shall be 0.40 percent, 2~~  
27 ~~percent shall be 0.80 percent, 4 percent shall be 1.6 percent, 6~~  
28 ~~percent shall be 2.4 percent, 8 percent shall be 3.2 percent, and 9.3~~  
29 ~~percent shall be 3.72 percent.~~

30 ~~(4) For any taxable year beginning on or after January 1, 2006,~~  
31 ~~and before January 1, 2007, 1 percent shall be 0.20 percent, 2~~  
32 ~~percent shall be 0.40 percent, 4 percent shall be 0.80 percent, 6~~  
33 ~~percent shall be 1.2 percent, 8 percent shall be 1.6 percent, and 9.3~~  
34 ~~percent shall be 1.86 percent.~~

35 ~~(5) For any taxable year beginning on or after January 1, 2007,~~  
36 ~~1 percent shall be 0 percent, 2 percent shall be 0 percent, 4 percent~~  
37 ~~shall be 0 percent, 6 percent shall be 0 percent, 8 percent shall be~~  
38 ~~0 percent, and 9.3 percent shall be 0 percent.~~

~~(j) (1) For purposes of this part, the term “taxable income of a nonresident or part-year resident” includes each of the following:~~

~~(A) For any part of the taxable year during which the taxpayer was a resident of this state (as defined by Section 17014), all items of gross income and all deductions, regardless of source.~~

~~(B) For any part of the taxable year during which the taxpayer was not a resident of this state, gross income and deductions derived from sources within this state, determined in accordance with Article 9 of Chapter 3 (commencing with Section 17031 and Chapter 11 (commencing with Section 17951):~~

~~(2) For purposes of computing “taxable income of a nonresident or part-year resident” under paragraph (1), the amount of any net operating loss sustained in any taxable year during any part of which the taxpayer was not a resident of this state shall be limited to the sum of the following:~~

~~(A) The amount of the loss attributable to the part of the taxable year in which the taxpayer was a resident.~~

~~(B) The amount of the loss which, during the part of the taxable year the taxpayer is not a resident, is attributable to California source income and deductions allowable in arriving at taxable income of a nonresident or part-year resident.~~

~~(3) For purposes of computing “taxable income of a nonresident or part-year resident” under paragraph (1), any carryover items, deferred income, suspended losses, or suspended deductions shall only be includible or allowable to the extent that the carryover item, deferred income, suspended loss, or suspended deduction was derived from sources within this state.~~

~~SEC. 2. Section 17062 of the Revenue and Taxation Code is amended to read:~~

~~17062. —(a) In addition to the other taxes imposed by this part, there is hereby imposed for each taxable year, a tax equal to the excess, if any, of—~~

~~(1) The tentative minimum tax for the taxable year, over~~

~~(2) The regular tax for the taxable year.~~

~~(b) For purposes of this chapter, each of the following applies:~~

~~(1) The tentative minimum tax is computed in accordance with Sections 55 to 59, inclusive, of the Internal Revenue Code, except as otherwise provided in this part.~~

~~(2) The regular tax is the amount of tax imposed by Section 17041 or 17048, before reduction for any credits against the tax, less any amount imposed under paragraph (1) of subdivision (d) and paragraph (1) of subdivision (e) of Section 17560.~~

~~(3) (A) The provisions of Section 55(b)(1) of the Internal Revenue Code are be modified to provide that the tentative minimum tax for the taxable year is equal to the following percent of so much of the alternative minimum taxable income for the taxable year as exceeds the exemption amount, before reduction for any credits against the tax:~~

~~(i) For any taxable year beginning on or after January 1, 1991, and before January 1, 1996, 8.5 percent.~~

~~(ii) For any taxable year beginning on or after January 1, 1996, and before January 1, 2003, 7 percent.~~

~~(iii) For any taxable year beginning on or after January 1, 2003, and before January 1, 2004, 5.6 percent.~~

~~(iv) For any taxable year beginning on or after January 1, 2004, and before January 1, 2005, 4.2 percent.~~

~~(v) For any taxable year beginning on or after January 1, 2005, and before January 1, 2006, 2.8 percent.~~

~~(vi) For any taxable year beginning on or after January 1, 2006, and before January 1, 2007, 1.4 percent.~~

~~(vii) For any taxable year beginning on or after January 1, 2007, 0 percent.~~

~~(B) In the case of a nonresident or part-year resident, the tentative minimum tax is computed by multiplying the alternative minimum taxable income of the nonresident or part-year resident, as defined in subparagraph (C), by a rate (expressed as a percentage) equal to the tax computed under subdivision (b) on the alternative minimum taxable income of the nonresident or part-year resident as if the nonresident or part-year resident were a resident of this state for the taxable year and as if the nonresident or part-year resident were a resident of this state for all prior taxable years for any carryover items, deferred income, suspended losses, or suspended deductions, divided by the amount of that income.~~

~~(C) For purposes of this section, the term “alternative minimum taxable income of a nonresident or part-year resident” includes each of the following:~~

1 (i) ~~For any period during which the taxpayer was a resident of~~  
2 ~~this state (as defined by Section 17014), all items of alternative~~  
3 ~~minimum taxable income (as modified for purposes of this~~  
4 ~~chapter), regardless of source.~~

5 (ii) ~~For any period during which the taxpayer was not a resident~~  
6 ~~of this state, alternative minimum taxable income (as modified for~~  
7 ~~purposes of this chapter) which were derived from sources within~~  
8 ~~this state, determined in accordance with Article 9 of Chapter 3~~  
9 ~~(commencing with Section 17301) and Chapter 11 (commencing~~  
10 ~~with Section 17951).~~

11 (iii) ~~For purposes of computing “alternative minimum taxable~~  
12 ~~income of a nonresident or part-year resident,” any carryover~~  
13 ~~items, deferred income, suspended losses, or suspended~~  
14 ~~deductions are allowable only to the extent that the carryover item,~~  
15 ~~suspended loss, or suspended deduction was derived from sources~~  
16 ~~within this state.~~

17 (4) ~~The provisions of Section 55(b)(2) of the Internal Revenue~~  
18 ~~Code, relating to alternative minimum taxable income, is modified~~  
19 ~~to provide that alternative minimum taxable income may not~~  
20 ~~include the income, adjustments, and items of tax preference~~  
21 ~~attributable to any trade or business of a qualified taxpayer.~~

22 (A) ~~For purposes of this paragraph, “qualified taxpayer”~~  
23 ~~means a taxpayer who meets both of the following:~~

24 (i) ~~Is the owner of, or has an ownership interest in, a trade or~~  
25 ~~business.~~

26 (ii) ~~Has aggregate gross receipts, less returns and allowances,~~  
27 ~~of less than one million dollars (\$1,000,000) during the taxable~~  
28 ~~year from all trades or businesses of which the taxpayer is the~~  
29 ~~owner or has an ownership interest, in the amount of that~~  
30 ~~taxpayer’s proportionate interest in each trade or business.~~

31 (B) ~~For purposes of this paragraph, “aggregate gross receipts,~~  
32 ~~less returns and allowances” means the sum of the gross receipts~~  
33 ~~of the trades or businesses that the taxpayer owns and the~~  
34 ~~proportionate interest of the gross receipts of the trades or~~  
35 ~~businesses that the taxpayer owns and of passthrough entities in~~  
36 ~~which the taxpayer holds an interest.~~

37 (C) ~~For purposes of this paragraph, “gross receipts, less returns~~  
38 ~~and allowances” means the sum of the gross receipts from the~~  
39 ~~production of business income, as defined in subdivision (a) of~~  
40 ~~Section 25120, and the gross receipts from the production of~~



~~nonbusiness income, as defined in subdivision (d) of Section 25120.~~

~~(D) For purposes of this paragraph, “proportionate interest” means:~~

~~(i) In the case of a passthrough entity that reports a profit for the taxable year, the taxpayer’s profit interest in the entity at the end of the taxpayer’s taxable year.~~

~~(ii) In the case of a passthrough entity that reports a loss for the taxable year, the taxpayer’s loss interest in the entity at the end of the taxpayer’s taxable year.~~

~~(iii) In the case of a passthrough entity that is sold or liquidates during the taxable year, the taxpayer’s capital account interest in the entity at the time of the sale or liquidation.~~

~~(E) (i) For purposes of this paragraph, “proportionate interest” includes an interest in a passthrough entity.~~

~~(ii) For purposes of this paragraph, “passthrough entity” means any of the following:~~

~~(I) A partnership, as defined by Section 17008.~~

~~(II) An S corporation, as provided in Chapter 4.5 (commencing with Section 23800) of Part 11.~~

~~(III) A regulated investment company, as provided in Section 24871.~~

~~(IV) A real estate investment trust, as provided in Section 24872.~~

~~(V) A real estate mortgage investment conduit, as provided in Section 24874.~~

~~(5) For taxable years beginning on or after January 1, 1998, Section 55(d)(1) of the Internal Revenue Code, relating to exemption amount for taxpayers other than corporations is modified, for purposes of this part, to provide the following exemption amounts in lieu of those contained therein:~~

~~(A) Fifty-seven thousand two hundred sixty dollars (\$57,260) in the case of either of the following:~~

~~(i) A joint return.~~

~~(ii) A surviving spouse.~~

~~(B) Forty-two thousand nine hundred forty-five dollars (\$42,945) in the case of an individual who is both of the following:~~

~~(i) Not a married individual.~~

~~(ii) Not a surviving spouse.~~

~~(C) Twenty-eight thousand six hundred thirty dollars (\$28,630) in the case of either of the following:~~

~~(i) A married individual who files a separate return.~~

~~(ii) An estate or trust.~~

~~(6) For taxable years beginning on or after January 1, 1998, Section 55(d)(3) of the Internal Revenue Code, relating to the phaseout of exemption amount for taxpayers other than corporations is modified, for purposes of this part, to provide the following phaseout of exemption amounts in lieu of those contained therein:~~

~~(A) Two hundred fourteen thousand seven hundred twenty-five dollars (\$214,725) in the case of a taxpayer described in subparagraph (A) of paragraph (5).~~

~~(B) One hundred sixty-one thousand forty-four dollars (\$161,044) in the case of a taxpayer described in subparagraph (B) of paragraph (5).~~

~~(C) One hundred seven thousand three hundred sixty-two dollars (\$107,362) in the case of a taxpayer described in subparagraph (C) of paragraph (5).~~

~~(7) For each taxable year beginning on or after January 1, 1999, the Franchise Tax Board shall recompute the exemption amounts prescribed in paragraph (5) and the phaseout of exemption amounts prescribed in paragraph (6). Those computations shall be made as follows:~~

~~(A) The California Department of Industrial Relations shall transmit annually to the Franchise Tax Board the percentage change in the California Consumer Price Index for all items from June of the prior calendar year to June of the current calendar year, no later than August 1 of the current calendar year.~~

~~(B) The Franchise Tax Board shall do both of the following:~~

~~(i) Compute an inflation adjustment factor by adding 100 percent to the percentage change figure that is furnished pursuant to subparagraph (A) and dividing the result by 100.~~

~~(ii) Multiply the preceding taxable year exemption amounts and the phaseout of exemption amounts by the inflation adjustment factor determined in clause (i) and round off the resulting products to the nearest one dollar (\$1).~~

~~(c) (1) (A) Section 56(a)(6) of the Internal Revenue Code as in effect on January 1, 1997, relating to installment sales of certain property, shall not apply to payments received in taxable years~~

beginning on or after January 1, 1997, with respect to dispositions occurring in taxable years beginning after December 31, 1987.

(B) This paragraph does not apply to taxable years beginning on or after January 1, 1998.

(2) Section 56(b)(1)(E) of the Internal Revenue Code, relating to standard deduction and deduction for personal exemptions not allowed, is modified, for purposes of this part, to deny the standard deduction allowed by Section 17073.5.

(3) Section 56(b)(3) of the Internal Revenue Code, relating to treatment of incentive stock options, is modified to additionally provide the following:

(A) Section 421 of the Internal Revenue Code does not apply to the transfer of stock acquired pursuant to the exercise of a California-qualified stock option under Section 17502.

(B) Section 422(e)(2) of the Internal Revenue Code applies in any case where the disposition and inclusion of a California-qualified stock option for purposes of this chapter are within the same taxable year and that section does not apply in any other case.

(C) The adjusted basis of any stock acquired by the exercise of a California-qualified stock option is determined on the basis of the treatment prescribed by this paragraph.

(d) The provisions of Section 57(a)(5) of the Internal Revenue Code, relating to tax-exempt interest do not apply.

(e) Section 57(a) of the Internal Revenue Code, relating to items of tax preference, is modified to include as an item of tax preference an amount equal to one-half of the amount excluded from gross income for the taxable year under Section 18152.5.

(f) The provisions of Section 59(a) of the Internal Revenue Code, relating to the alternative minimum tax foreign tax credit, do not apply.

SEC. 3.—This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.